

Factsheet 28 February 2022

# NIKKO AM NZ CASH STRATEGY

Assets are held in the Nikko AM Wholesale NZ Cash Fund. The Nikko AM NZ Cash Fund (retail) and Nikko AM KiwiSaver Scheme NZ Cash Fund invest in units in the wholesale fund, which the commentary refers to.

## Market Overview

- The Reserve bank lifted the OCR by 0.25%, in line with consensus, taking the OCR to 1%.
- Statements and forecasts made by the Reserve Bank were Hawkish, showing growing concern around the risk of high inflation becoming embedded.
- The Reserve Bank increased its OCR track by 0.74% from its November statement, now seeing peak OCR at 3.35% in early 2023.

## Fund Highlights

- The fund holds a longer than benchmark duration position to benefit from slope in the credit and bank bill curves.
- Duration is actively managed with fund positions reflecting the likely path of the OCR over the coming months along with what is priced into security yields.
- The fund holds a range of securities including floating rate notes which provide some protection against a rising cash rate.

## Performance

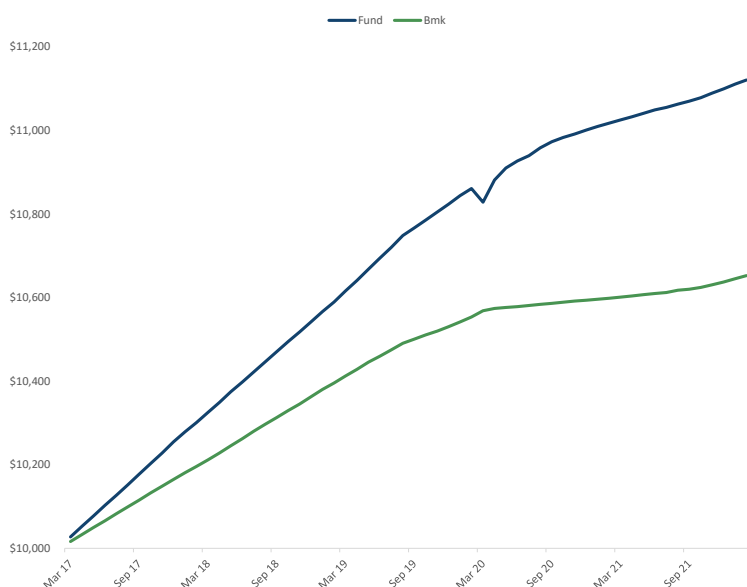
	One month	Three months	One year	Three years (p.a)	Five years (p.a)	Ten years (p.a)
Wholesale <sup>1</sup>	0.09%	0.28%	0.94%	1.65%	2.15%	3.02%
Benchmark <sup>2</sup>	0.07%	0.21%	0.51%	0.82%	1.27%	2.08%
Retail <sup>3</sup>	0.07%	0.22%	0.66%	1.33%	1.81%	
KiwiSaver <sup>3</sup>	0.06%	0.19%	0.52%	1.28%		

1. Returns are before tax and before the deduction of fees.

2. Benchmark: Bloomberg NZBond Bank Bill Index. No tax or fees.

3. Returns are before tax and after the deduction of fees and expenses and including tax credits (if any).

## Five Year Cumulative Performance, \$10,000 invested<sup>1, 2</sup>



## Portfolio Manager

**Fergus McDonald,**

**Head of Bonds and Currency**

Fergus is responsible for the investment of the Bond, Cash and Currency mandates. Fergus has been actively involved in the NZ financial markets since 1981. The portfolio management team for the domestic fixed income funds includes Ian Bellew, Fixed Income Manager and Matthew Johnson, Fixed Income Manager.



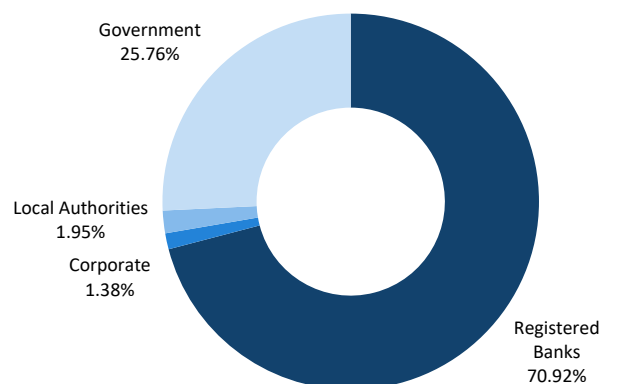
## Overview

The strategy aims to generate income by constructing an actively managed investment portfolio of short-term deposits and bonds whilst preserving capital value.

## Objective

The fund aims to outperform the benchmark return by 0.20% per annum before fees, expenses and taxes over a rolling three year period.

## Asset Allocation



Top 5 Issuers	(%)	Credit Quality	(%)	Duration
Westpac New Zealand Ltd	16.13	AAA	25.8	Fund 99 days vs Benchmark 45 days
NZ Tax Trading Co	12.60	AA	41.0	
Tax Management NZ Limited	12.55	A	33.2	
ANZ Bank New Zealand	9.60			<b>Yield to Maturity</b>
Kiwibank Ltd	7.91			Fund (gross) 1.66% vs Benchmark 1.12%

### Market Commentary

The key event of February was the Reserve Bank’s Monetary Policy Statement (MPS). Prior this meeting consensus expectations were for a 25bps hike to be delivered, although OIS pricing suggested some market participants expected a larger 50bps increase. A 25bps hike was delivered in line with general market expectations taking the OCR to 1%, however accompanying forecasts and statements revealed a decidedly hawkish bias. The Reserve Bank stated their decision between a 25bps and 50bps hike was “finely balanced” and that they were prepared to move in bigger steps than 25bps “if required”.

Most notable among the Reserve Bank’s economic projections was an uplift in their inflation forecasts - particularly for 2022 where they were increased by roughly 1% whilst 2023 and 2024 received more modest uplifts of circa 0.2%. They forecast peak CPI inflation of 6.6% which is expected to occur in the first quarter of 2022 before fading towards 4% by year end. With such robust inflation it is unsurprising that the Reserve Bank’s statement now acknowledges inflation as the “most significant risk to be avoided” a key change to prior statements where inflation was viewed purely as a temporary aberration. In keeping with these concerns the Reserve Bank increased its OCR track by 0.74% from its November statement, now seeing peak OCR at 3.35% in early 2023 (higher than pre MPS market expectations of around 3%).

The Reserve Bank’s Monetary Policy Statement also revealed it will begin to run down its QE bond holdings through bond maturities and managed NZGB sales to the New Zealand Debt Management office. Sales are expected to total \$5b per fiscal year (~100m per week). The bank explicitly stated that the OCR is its key monetary policy tool, and expect the impact of this Quantitative Tightening to be “very small”.

Overall, this more Hawkish stance has seen interest rates continue to move up particularly for terms longer than one year given the higher than expect peak OCR forecast. The market continues to view 25bps increases at each of the banks 2022 meetings as the most likely outcome, however some credence has now been given to the potential for 50bps moves – previously seen as unlikely given the statements in the Reserve Bank’s “he Kōtuku” least regrets approach speech of 2021. This has resulted in market pricing front loading OCR increases whilst continuing to price roughly a 25bps increase at each meeting of 2022.

### Fund Commentary

The fund performed well in February returning 0.09% outperforming the 90-day bank bill index which returned 0.07%. Reserve Bank statements indicate an increased willingness to move the OCR by more than 25bps at any meeting, however we continue to view the hurdle of it doing so as high. Market pricing reflects this risk with cash rate rises expected at each meeting of 2022 with some front end loaded risk of 50bps moves. We note key interest rates have moved up significantly since late last year, most notably 1- and 2-year swap rates which feed through to domestic mortgage rates. The slowing impetus of these increased mortgage rates and interest rates in general will increasingly take hold over 2022 elevating the potential for the economy to slow and inflation to recede sooner than expected. We continue to implement a barbel investment strategy to exploit this pricing.

Key Fund Facts			
<b>Distributions</b>		<b>Estimated annual fund charges (incl. GST)</b>	
Wholesale fund:	Calendar quarter	Wholesale:	Negotiated outside of unit price
Retail fund:	Calendar quarter	Retail:	0.30%, refer PDS for more details
KiwiSaver fund:	Does not distribute	KiwiSaver:	0.45%, refer PDS for more details
<b>Hedging</b>		<b>Buy / Sell spread</b>	<b>Strategy size</b>
All investments will be in New Zealand dollars		0.00% / 0.00	\$827.3m
<b>Strategy Launch</b>			
October 2007			
<b>Restrictions</b>			
Adult entertainment, gambling, fossil fuels, alcohol stocks, tobacco stocks. For more information please refer to the Statement of Investment Policy and Objectives (SIPO) which can be found on our website <a href="https://www.nikkoam.co.nz/invest/retail">https://www.nikkoam.co.nz/invest/retail</a> .			
<b>Exclusions</b>			
Securities that conduct activities listed on the Schedule to Cluster Munitions Prohibition Act 2009.			

### Compliance

The wholesale fund complied with its investment mandate and trust deed during the month.

### Contact Us

[www.nikkoam.co.nz](http://www.nikkoam.co.nz) | [nzenquiries@nikkoam.com](mailto:nzenquiries@nikkoam.com)

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